

ST 98-5

Tax Type: SALES TAX

Issue: Responsible Corp. Officer - Failure to File or Pay Tax

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
SPRINGFIELD, ILLINOIS**

THE DEPARTMENT OF REVENUE)	
OF THE STATE OF ILLINOIS)	
)	Docket #
v.)	IBT #
)	NPL #
TAXPAYER)	
Respondent)	

RECOMMENDATION FOR DISPOSITION

Appearances: Joseph E. McMenamin, Dunn & McMenamin, for TAXPAYER; Charles Hickman, Special Assistant Attorney General, for the Department of Revenue of the State of Illinois.

Synopsis:

The Illinois Department of Revenue (hereinafter referred to as the "Department") issued a Notice of Penalty Liability to TAXPAYER (hereinafter referred to as "TAXPAYER" or the "Respondent") pursuant to section 13½ of the Retailers' Occupation Tax Act¹. The basis of the notice was that the respondent was a responsible officer for the tax liabilities incurred by CORPORATION. The respondent timely protested the notice and requested a hearing in the matter. At the hearing, it was established that the respondent was a responsible officer of the

¹. The liability for Retailer's Occupation Taxes herein accrued in 1987 and 1988. Therefore, the statute which applies is Ill. Rev. Stat. ch. 120, ¶ 452½ § 13½. The Uniform Penalty and Interest Act (UPIA), at 35 ILCS 735/3-7, which provides for a personal liability penalty for responsible officers of corporations, is the current replacement provision. The UPIA is effective for taxes incurred on January 1, 1994 and later.

corporation who had not willfully failed to pay some of the taxes at issue to the Department. It is therefore recommended that the decision of the Director of the Department be that this matter be resolved partly in favor of the respondent and partly in favor of the Department.

Findings of Fact:

1. The *prima facie* case of the Department, consisting of Notice of Penalty Liability number XXXX issued to the respondent on November 22, 1989 in the amount of \$56,569.00, was established by the admission into evidence of Department's Exhibit No. 1. (Tr. p. 19)

2. CORPORATION (hereinafter the "Corporation") was in the business of selling new and used mobile homes and providing setup services for the homes. (Tr. p. 22)

3. The respondent was the president and general manager of the corporation. (Tr. p. 22)

4. During the time that the corporation was in business, the respondent was responsible for mailing the sales tax returns. The office manager would prepare the paper work. The respondent would then review it, sign it, sign any accompanying check, and forward the return to the Department. (Tr. p. 59)

5. Notice of Penalty Liability number XXXX (hereinafter referred to as the "NPL") was issued to TAXPAYER as the responsible officer of the corporation for the periods, as listed on the notice, of November 1987, April 1988, July 1988, and October 1988. The notice was for the amount of \$56,569.34 including interest through November 22, 1989. (Dept. Ex. 1 p. 2; Respondent Ex. No. 1; Respondent Ex. No. 3 p. 2)

6. The basis of the NPL is six assessments for which the Department seeks to hold the respondent liable. The assessments are: K284523 for \$31,429.07 in tax, period covered according to the notice, 11/87; U250915 for \$2,908.12 in tax, period covered according to the notice, 11/87; V255248 for \$1,729.95 in tax, period covered according to the notice, 11/87; V255688 for \$2,870.32 in tax, period covered according to the notice, 4/88; V256261 for \$270.05 in tax, period covered according to the notice, 7/88; and U251283 for \$1477.81 in tax, period covered according to the notice, 10/88. (Tr. p. 13; Dept. Ex. No. 3; Respondent Ex. No.

1; Respondent Ex. No. 3 p. 2)

7. Each of the assessments are composed of liabilities compiled from returns for sales of mobile homes. A mobile home sale is documented with the Department on a RR-556 form. The forms are the property of the State that are issued by the Department. All forms must be accounted for by the Department. (Dept. Grp. Ex. No. 3; Respondent's Grp. Ex. No. 3; Respondent's Ex. No. 4; Tr. pp. 83-84)

8. Assessment K284523 is tabulated from twenty-four RR-556 returns. Of the twenty-four returns, the signature of the taxpayer is not present on four of the returns. On all of the 24 returns, in a box in the upper right hand corner labeled "official use", are identical initials, the date of 11/23/87, the number 87337, which coincidentally is the Julian date for November 23, 1987, and a sequential number from 3200300 through 3200326 with the exceptions of numbers 3200313, -19 and -21. (Dept. Grp. Ex. No. 3 pp. 5, 17, 22 & 40; Respondent's Grp. Ex. No. 3 pp. 6, 18, 23 & 40)

9. Assessment U250915 consists of two returns². The respondent's signature is not present on one of the returns. In the boxes in the upper right hand corner of the forms, labeled "official use", are the same initials as found in the prior returns, the date of 11/23/87, the same number 87337, and sequential numbers 3200319 and 3200321. (Dept. Grp. Ex. No. 3 pp. 53-58; Respondent's Grp. Ex. No. 3 pp. 53-58)

10. Assessment V255248 consists of one return. The respondent's signature is present on the return. On the return, the box in the upper right hand corner labeled "official use" contains the same initials as found in the prior returns, the date of 11/23/87, the same number 87337, and sequential number 3200313. (Dept. Grp. Ex. No. 3 p. 62; Respondent's Grp. Ex. No. 3 p. 62)

11. Assessment V255688 consists of two returns. The respondent's signature is not

2. In the summation of the transactions prepared by the taxpayer, found at Respondent's Ex. No. 3 p. 1, the taxpayer listed only one return for assessment number U250915. It is assumed the error was made because only one of the returns involved with the assessment number had no signature of the respondent.

present on either of the returns. In the box on the upper right hand corner of the returns is 88125, which coincidentally is the Julian date for May 5, 1988. (Dept. Grp. Ex. No. 3 pp. 66 & 68 ; Respondent's Grp. Ex. No. 3 pp. 66 & 68)

12. Assessment V256261 consists of one return. The respondent's signature is present on the return. ((Dept. Grp. Ex. No. 3 p. 72 ; Respondent's Grp. Ex. No. 3 p. 72)

13. Assessment U251283 consists of one return. The respondent's signature is not present on the return. In the box on the upper right hand corner of the return is the number 88301 which coincidentally is the Julian date of October 28, 1988. (Dept. Grp. Ex. No. 3 p. 76; Respondent's Grp. Ex. No. 3 p. 76)

14. The returns that were signed represent sales of mobile homes that took place. (Tr. p. 42)

15. The corporation filed a Chapter 7 bankruptcy petition on November 20, 1987. On January 8, 1988, the Department filed a proof of claim for taxes due in the amount of \$35,571.17. (Respondent's Ex. No. 7)

16. It was the respondent's belief that there would be enough money available from the bankruptcy trustee to pay all liabilities due the Department. (Tr. p. 41)

17. The Department received \$13,191.43 from the bankruptcy trustee. That amount was applied to assessment K-284523. (Tr. p. 65)

18. The bankruptcy trustee did not have sufficient funds to pay all debts due to the creditors of the corporation. (Tr. pp. 66-68)

19. On August 6, 1992, a special assistant attorney general for the Department issued a notice of demand for documentary evidence to the respondent regarding NPL number XXXX. The demand was for "any and all documentary evidence to support the Taxpayer's claim to an exemption and/or refund or credit from Illinois taxes." The notice gave the taxpayer sixty days to produce the evidence. (Dept. Ex. 2 pp. 3)

20. In 1992, the respondent did not have legal counsel. (Tr. p. 104)

21. TAXPAYER responded to the notice of demand by a telephone call to the special

assistant attorney general. The respondent requested a change of venue to the Department's Springfield office of administrative hearings. (Tr. pp. 29-31)

Conclusions of Law:

The Department seeks to hold the respondent personally liable for taxes which were incurred by the corporation. The imposition of such liability was authorized by paragraph 452½ of the Retailers' Occupation Tax Act in 1987 and 1988, the taxable years in question. That portion of the statutes stated:

Failure to file return or pay taxes-Liability of corporate officers or employees

§ 13½. Any officer or employee of any corporation subject to the provisions of this Act who has the control, supervision or responsibility of filing returns and making payment of the amount of tax herein imposed . . . and who willfully fails to file such return or make such payment to the Department . . . shall be personally liable for a penalty equal to the total amount of tax unpaid by the corporation, including interest and penalties thereon; . . .

An officer or employee of a corporation may therefore be held personally liable for the corporation's taxes if (1) the individual had the control, supervision or responsibility of filing the returns and paying the taxes and (2) the individual willfully failed to perform these duties.

Under §13½, the Department's certified record relating to the penalty liability constitutes *prima facie* proof of the correctness of the penalty due³. See Branson v. Department of Revenue, 168 Ill.2d 247, 260 (1995). Once the Department has presented its *prima facie* case, the burden

³. The relevant portion of the statute at §13½ states:

The Department shall determine a penalty due under this Section according to its best judgment and information, and such determination shall be *prima facie* correct and shall be *prima facie* evidence of a penalty due under this Section. Proof of such determination by the Department shall be made at any hearing before it or in any legal proceeding by reproduced copy of the Department's record relating thereto in the name of the Department under the certificate of the Director of Revenue. Such reproduced copy shall, without further proof, be admitted into evidence before the Department or any legal proceeding and shall be *prima facie* proof of the correctness of the penalty due, as shown thereon. Ill.Rev.Stat. 1987, ch. 120, ¶452½.

shifts to the respondent to establish that one or more of the elements of the penalty are lacking, i.e., that the person charged was not the responsible corporate officer or employee, or that the person's actions were not willful. Id. at 261. In order to overcome the Department's *prima facie* case, the allegedly responsible person must present more than his or her testimony denying the accuracy of the Department's assessment. A. R. Barnes & Co. v. Department of Revenue, 173 Ill.App.3d 826, 833-34 (1st Dist. 1988). The person must present evidence that is consistent, probable, and identified with books and records to support the claim. Id.

In this case, the Department's *prima facie* case was established when the Department's certified record relating to the penalty liability was admitted into evidence. In response, TAXPAYER admitted that he was the person responsible for filing the returns for the corporation. He also admitted that the RR-556 returns that he signed represented sales of mobile homes that took place and for which he was responsible for the tax.

Therefore, the first question before me is whether the failure of the respondent to pay the taxes for the eight unsigned returns was willful.

In interpreting the statutory language, the courts have used such words as "consciously", "voluntarily", "intentionally", "knowingly" and "recklessly" in the attempt to define what is a willful attempt for failure to evade or defeat the tax due. The Illinois Supreme Court has sought guidance from cases interpreting §6672 of the Internal Revenue Code (26 U.S.C. §6672)⁴ in its quest to interpret the word willful. See Branson at 254-256; Department of Revenue v. Heartland Investment's Inc., 106 Ill.2d 19, 29-30 (1985). These cases define willful as involving intentional, knowing, and voluntary acts or, alternatively, reckless disregard for obvious known risks. Id. Willful conduct does not require bad purpose or intent to defraud the government. Branson at 255; Heartland at 30. Willfulness may be established by showing that the responsible person (1) clearly ought to have known that (2) there was a grave risk that the taxes were not being paid and (3) the person was in the position to find out for certain very easily. Wright v.

⁴. The section imposes personal liability on corporate officers who willfully fail to collect, account for, or pay over, employees' social security and Federal income withholding taxes.

United States, 809 F.2d 425, 427 (7th Cir 1987). Furthermore, whether the person in question willfully failed to pay the taxes at issue is a matter of fact to be determined on the basis of the evidence in each particular case. Heartland at 30; Department of Revenue v. Joseph Bublick & Sons, Inc., 68 Ill.2d 568, 577 (1977).

In the present case, the respondent argued that there was no willful attempt to avoid paying taxes on returns that were presented to the Department after the corporation had filed bankruptcy. Once the corporation filed bankruptcy, the assets of the corporation were in the hands of the trustee and the respondent could not, by law, control the corporation. The respondent asserts that the returns submitted were never signed by him and did not reflect transactions that ever took place. I find that his testimony is believable regarding the eight unsigned returns.

In Department of Revenue v. R. S. Dombrowski Enterprises, Inc., 202 Ill.App.3d 1050 (1st Dist. 1990; rehearing denied, May 1, 1990) the Appellate Court found that the merits of a final assessment, that is the basis of an NPL, may not be reviewed at the hearing on the NPL. (No jurisdiction to review the accuracy of an assessment once it becomes final). In the instant case, the attorney for the taxpayer was precluded at the hearing, pursuant to the 60 day demand notice for documentary evidence, from admitting evidence regarding the accuracy of the amounts of the underlying assessments. However, the evidence at the hearing did establish a lack of willfulness to remit tax on the part of the respondent regarding the eight unsigned returns at issue.

There are thirty-one returns that form the basis of the liability at issue. TAXPAYER admitted responsibility for the returns that he signed. Of the remaining eight returns which are unsigned, portions of the returns are not legible. As a matter of fact, many of the returns that were signed did not contain the date of delivery, any dealer's invoice number, the dealer's stock number, whether the item sold was new, used, or a demo, the year of the vehicle, or even the vehicle identification number.

The respondent asserted that a departmental auditor came to his home and took the RR-

556 forms from the TAXPAYER's garage after the corporation had declared bankruptcy. Unfortunately, TAXPAYER did not have the auditor appear at the hearing to corroborate this statement. It has been at least ten years since the alleged incident. The respondent was involved with a bankruptcy of his business and he and his wife were eventually forced to file for personal bankruptcy.

I certainly find it unusual that the first twenty-seven of the thirty-one returns that form the basis of the NPL at issue have the same Julian date in the "official use" box, contain the same initials, and have sequential numbers. It adds credibility to the statement by the respondent that the returns were taken from his home.

I also find that the respondent himself was credible. His testimony was that he was responsible for the payments to the Department of sales that, in fact, took place and were represented by the twenty-three signed returns. He asserts that he had no knowledge that the eight unsigned returns were true sales of motor homes. I find that the taxpayer's failure to pay those taxes was not willful.

Regarding the assertion that there was no willful failure to pay the taxes due regarding the twenty-three signed returns, I find that the taxpayer's reliance on the trustee of the corporation's bankruptcy to pay that liability is not sufficient to overcome the *prima facie* case of the Department. TAXPAYER had knowledge of the liability and access to the corporate funds at the time the liabilities occurred. He admitted that they were valid sales of motor homes. While the returns were submitted to the Department after the corporate bankruptcy, the sales took place prior to the corporation filing the bankruptcy petition. A taxpayer may not prefer other creditors over the Department to avoid a liability that is due. If a responsible corporate officer used collected Retailers' Occupation Taxes to pay other creditors of the corporation, while knowing that he or she was obligated to file returns and remit taxes, the willfulness element of the NPL is satisfied. Branson, *supra.*, See also, Verdung v. U.S., 84-1 USTC 9324 (N.D. Ill. 1983).

I therefore recommend that the portion of NPL number XXXX relating to the eight returns that the taxpayer did not sign, in the amount of \$11,115.38 of tax, be dismissed. I also

recommend that the remainder of the NPL, in the amount of \$29,569.94 of tax, be upheld, with deductions made for the payment by the trustee of the bankruptcy.

Respectfully Submitted,

Barbara S. Rowe
Administrative Law Judge
March 6, 1998